Supreme Court, U.S.
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No. 98-192

IN THE

Supreme Court of the United States

OCTOBER TERM, 1998

LARRY CHANDLER and JOANNE CHANDLER,
Petitioners,

VS.

NORWEST BANK MINNESOTA, NATIONAL ASSOCIATION and CUSTOM MORTGAGE INC.,
Respondents.

On Petition for a Writ of Certiorari to the
United States Court of Appeals for the Eighth Circuit

RESPONDENT NORWEST'S BRIEF IN OPPOSITION

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QUESTIONS PRESENTED FOR REVIEW

1. Was the Eighth Circuit correct in affirming summary judgment in favor of Norwest, given Norwest's demonstrated lack of involvement in the Chandlers' loan transaction?

2. Was the Eighth Circuit correct in finding that Custom's sale of the Chandlers' loan to Equicon after closing constituted a "secondary market" transaction, exempt from Section 8 of the Real Estate Settlement Procedures Act?

3. Was the Eighth Circuit correct in affirming the District Court's imposition of Rule 11 sanctions upon the Chandlers' attorneys, given their failure to investigate the facts against Norwest prior to filing this action?

PARTIES TO THE PROCEEDING

The petition accurately lists the parties to the proceedings.

Norwest Bank Minnesota, N.A. lists its parent companies and non-wholly owned subsidiaries as follows:

Parent Company
Norwest Corporation

Non-Wholly Owned Subsidiaries
Crestone Capital Management, Inc.
Commonwealth Leasing Corporation

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ADDITIONAL STATUTES AND REGULATIONS INVOLVED

Missouri Revised Statutes, Liability of Trustee To Third Persons, § 456.480.

. . .

2. A trustee is individually liable for obligations arising from ownership or control of the trust assets or for torts committed in the course of administration of the trust only if he is personally at fault.

. . .

Regulation X, 24 C.F.R. Part 3500
Appendix B

The following illustrations provide additional guidance on the meaning and coverage of the provisions of RESPA....

. . .

5. *Facts:* A, a "mortgage originator," receives loan applications, funds the loans with its own money or with a wholesale line of credit for which A is liable, and closes the loans in A's own name. Subsequently, B, a mortgage lender, purchases the loans and compensates A for the value of the loans, as well as for any mortgage servicing rights.

Comments: Compensation for the sale of a mortgage loan and servicing rights constitutes a secondary market transaction, rather than a referral fee, and is beyond the scope of section 8 of RESPA. For purposes of section 8, in determining whether a *bona fide* transfer of the loan obligation has taken place, HUD examines the real source of funding, and the real interest of the named settlement lender.

. . .

STATEMENT OF THE CASE

Few opinions of a United States court of appeals merit less consideration on a petition for a writ of certiorari than the opinion in this case. Simply stated, the Chandlers seek review of a decision that is based squarely on and affirms a finding of fact by the District Court about Norwest's lack of involvement in the Chandlers' loan transaction. No amount of rhetoric in their brief can make these findings, supported by substantial evidence, worthy of a writ of certiorari.

The Chandlers' primary argument with respect to Norwest is that the Eighth Circuit misapplied Fed.R.Civ.P. 11 when it affirmed the imposition of sanctions against their attorneys for their failure to investigate the facts prior to filing this lawsuit. This is not a proper basis for a petition for certiorari (see Supreme Court Rule 10) and, even if it were, the Chandlers' Petition necessarily fails, because the Eighth Circuit properly reviewed the District Court's decision under the abuse-of-discretion standard mandated by *Cooter & Gell v. Hartmarx Corp.*, 496 U.S. 384, 405, 110 S. Ct. 2447, 110 L.Ed. 2d 359 (1990).

Factual Background:

Petitioners, Larry and Joanne Chandler ("the Chandlers"), brought this putative class action under Section 8 of the Real Estate Settlement Procedures Act ("RESPA"), 12 U.S.C. § 2607, against Norwest Bank Minnesota ("Norwest") and Custom Mortgage, Inc. ("Custom"), the originator of their mortgage loan. The Chandlers allege that their loan was "table funded," thus bringing the transaction under the coverage of RESPA § 8.[1] The Chandlers specifically assert that Norwest, prior to closing, purchased their loan from Custom, and in the process, paid

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[1] Under RESPA, "table funding" means "a settlement at which a loan is funded by a contemporaneous advance of loan funds and an assignment of the loan to the person advancing the funds. . . ." 24 C.F.R. § 3500.2(b).

excessive and unearned fees. However, the evidentiary record unequivocally demonstrates that Norwest never purchased the Chandler loan.

On the contrary, Equicon Corporation ("Equicon," a/k/a "Access") — not Norwest — purchased the Chandler loan from Custom after closing. At the direction of Equicon, Custom then assigned the loan to Norwest, as trustee of the Equicon Loan Purchase Trust ("the Trust), for deposit into the Trust. As trustee, Norwest's duties were primarily to be the custodian of the mortgage loan documents Equicon purchased from Custom and other lenders. Norwest has never had any beneficial ownership interest in the mortgages in the trust. (Pet. App. 4). Norwest did not (and indeed, had no reason to) pay, receive or determine any of the fees Equicon paid to Custom. Therefore, even if the Chandlers had a colorable claim under RESPA (which they do not because their loan was not "table funded"), the violation was necessarily committed by parties other than Norwest. Had the Chandlers' attorneys investigated the facts prior to filing the complaint, they would have known that Norwest is not a proper defendant.

Procedural Background:

For these reasons, the District Court granted Norwest's motion for summary judgment and ordered the Chandlers' attorneys to pay Norwest's attorneys' fees. "Although plaintiffs *may* have arguably had a reasonable belief that their claim against Custom had or was likely to have evidentiary support," wrote the District Court, "they could not have made any reasonable inquiry as to Norwest, given Norwest's uninvolvement in the actual transaction." (Pet. App. 22) (emphasis in original).

On appeal before the Eighth Circuit, a majority of the panel (Circuit Judges Bowman and Loken) (hereinafter, "the Majority") reached precisely the same conclusion:

> [T]he loan was sold by Custom to Equicon, *not* Norwest... We agree with the District Court that the Chandlers failed to produce *even a scintilla of evidence* that Norwest was involved in their mortgage loan transaction in any capacity other than as trustee of the Equicon Trust.

(Pet. App. 8 & 9) (emphasis added). The Majority additionally held that the Chandlers "failed to produce any evidence" that their mortgage loan was "table funded" by Custom. (Pet. App. 7-8). Accordingly, it affirmed summary judgment in favor of Norwest and Custom, as well as the District Court's imposition of Rule 11 sanctions against the Chandlers' attorneys.

Although Circuit Judge Gibson dissented, his primary factual finding with respect to the "table funding" issue confirms that Equicon rather than Norwest actually purchased the Chandler loan from Custom: "I believe," he wrote, "that the 'real source of funding' for the Chandlers' loan was *Equicon*...." (Pet. App. 12) (emphasis added). Judge Gibson went on to say that Equicon acted "on behalf of Norwest" when it purchased the Chandler loan. (Pet. App. 12). But there is nothing in the evidentiary record to support this remark. Neither is there anything in RESPA or the common law of trusts to suggest that when a trust owner like Equicon acquires property for the trust, it does so on behalf of the trustee, individually or otherwise. Accordingly, the Eighth Circuit properly denied the Chandler's Suggestion for Rehearing en Banc and Rehearing by the Panel. (Pet. App. 14).

Nevertheless, the Chandlers seize upon this portion of Judge Gibson's dissent as vindication for their legally indefensible position: that RESPA contemplates holding a trustee strictly liable for the alleged misconduct of third parties with respect to a trust asset (necessarily committed prior to the asset's deposit into the trust). However, neither RESPA nor Judge Gibson's dissent support this position. The Chandlers' unfounded argument hardly constitutes an "important question of federal law" worthy of a writ of certiorari. *See* Supreme Court Rule 10.

REASONS FOR DENYING THE WRIT

1. THE EIGHTH CIRCUIT CORRECTLY AFFIRMED SUMMARY JUDGMENT IN FAVOR OF NORWEST.

A. Norwest's Status As a Mere Trustee Is Not Sufficient to Trigger RESPA Liability.

Throughout their appellate briefs and Petition for Certiorari, the Chandlers concede Norwest's lack of involvement in the purchase and sale of their loan between Custom and Equicon. Instead, they argue that Norwest's status as a mere trustee is sufficient to trigger RESPA liability. (Pet., pp.18-19). In support, the Chandlers cite the RESPA provision defining "persons" as "individuals, corporations, associations, partnerships and trusts." 12 U.S.C. § 2602(5). The Chandlers reason that because Norwest "is a 'person' as defined by RESPA," it may be held individually liable under the Act, even if Norwest neither paid, received, nor determined the allegedly excessive fees which Equicon paid to Custom. (Pet., p.19). A holding to the contrary, the Chandlers assert, would "silently rewrite[] RESPA to include a trustee exception." (Pet., p. 18).

Norwest respectfully suggests that the Chandlers' argument aptly demonstrates the propriety of Rule 11 sanctions in this case. The simple fact that Norwest qualifies as a "person" under the Act hardly constitutes probative evidence of a RESPA § 8 violation. Courts interpret Section 8 to mean that unless the defendant gives, receives, or determines a portion of the disputed fee, no relief is available under this section of the Act.[2] RESPA § 8 does *not* provide borrowers a "no-fault" cause of action against any "person," whether that "person" be an "individual," a "corporation," or a trustee like Norwest. The Chandlers do not,

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[2] *See, e.g., In re Davis,* 172 B.R. 437, 467 (Bankr. D. Dist. Col. 1994); *McCarrick v. Polonia Federal Sav. and Loan Ass'n.*, 502 F. Supp. 654, 657 (E.D. Pa. 1980).

and cannot possibly, cite any authority in support of their extraordinary theory of RESPA liability.

The Chandlers' reference to the common law of trusts does not change the analysis. The Chandlers argue that under Missouri law, Norwest's bare legal title as trustee is reason enough to hold it individually liable under RESPA. (Pet., p.19) ("Because a trustee owns legal title to the trust property there is absolutely no support for the majority's *assumption* that Norwest, as a trustee, is not [liable under] RESPA") (emphasis in original). But the Chandlers fail to cite any authority in support of this astounding proposition. They also neglect to distinguish (much less discuss) case law and statutes like Mo. Rev. Stat. § 456.480 which govern a trustee's liability to third persons like the Chandlers. That statute provides in pertinent part:

> A trustee is individually liable for obligations arising from ownership or control of the trust assets or for torts committed in the course of administration of the trust *only if he is personally at fault.*

Mo. Ann. Stat. § 456.480.2 (Vernon 1992) (emphasis added).

In short, the Chandlers have absolutely no basis to argue that Missouri's law on trusts contemplates holding a trustee *strictly* liable for the alleged misconduct of third parties. Simply because the trustee holds "legal" title to the trust property does not trigger RESPA § 8 liability. There is no need for this Court to review the Eighth Circuit's proper rejection of the Chandlers' unfounded theory on a writ of certiorari.

B. The Eighth Circuit Correctly Rejected the Chandlers' Allegation that Equicon Purchased Their Loan from Custom "On Behalf of Norwest."

The Chandlers alternatively argue that Norwest is *vicariously* liable for Equicon's alleged RESPA violation, asserting that when Equicon paid the purportedly excessive fee to Custom, it

did so as an "agent" of Norwest." (Pet., p.14) ("Norwest, through its agent Equicon agreed to fund the Chandlers' loan.") (emphasis omitted). The Chandlers' only purported "evidence" of this "agency" relationship are two sections in the Purchase and Sale Agreement between Equicon, Custom and Norwest. (Pet., p.6). These sections provide in pertinent part:

> *SECTION 1. Purchase and Sale of Loans*: [Custom] shall convey, sell, assign, transfer and deliver to *Trustee, on behalf of the Trust* all of [Custom's] right, title and interest in the Loans. . . .
>
> *SECTION 4. Purchase Price:* [Equicon], *on behalf of the Trustee,* will wire transfer the Purchase Price pursuant to [Custom's] written instructions on the Settlement Date. (emphasis added).

The Chandlers assert that Sections 1 and 4 of the Agreement prove that when Equicon paid Custom in exchange for their mortgage loan, the money was actually paid "on behalf of Norwest." (Pet., p.7). On the contrary, the Agreement irrefutably corroborates Norwest's position in all respects; namely, that when Equicon purchased the Chandler loan from Custom, it did so "*on behalf of the Trust*" and not on behalf of Norwest. The Chandlers failed to present any evidence whatsoever to contradict the "plain meaning" of these two provisions. Indeed, it makes no sense to say that Equicon — the *owner* of the Trust — committed the alleged RESPA violation "on behalf of Norwest," when the evidentiary record (and the common law of trusts) unequivocally proves that Norwest acquired no beneficial interest in the Chandler loan. *See also* BOGERT TRUSTS & TRUSTEES § 731 at 363 (Rev. 2d ed. 1982) ("*Obviously* a trustee is *not* liable for the torts of the settlor.") (emphasis added). Accordingly, the Majority soundly rejected the Chandlers' unfounded interpretation of the Agreement:

> The Purchase and Sale Agreement *cannot and does not* raise a material question of fact necessary to defeat a summary judgment motion. The District Court did not err in granting summary judgment to Norwest and Custom.

(Pet. App. 8) (emphasis added). The Dissent neither discussed nor directly contested this dispositive, factual finding. The Chandlers' Petition for Certiorari should be denied. *See* Supreme Court Rule 10 ("A petition for a writ of certiorari is *rarely granted* when the asserted error consists of erroneous factual findings....") (emphasis added).

2. THE EIGHTH CIRCUIT CORRECTLY HELD THAT EQUICON'S PURCHASE OF THE CHANDLER LOAN AFTER CLOSING WAS AN EXEMPT "SECONDARY MARKET" TRANSACTION.

The Eighth Circuit correctly recognized that while "table funded" transactions are subject to RESPA § 8, "secondary market transactions" are not. (Pet. App. 7). *See* 24 C.F.R. § 3500.5(b)(7); 24 C.F.R. Part 3500, Appendix B. Accordingly, unless the Chandlers presented sufficient evidence that their loan was simultaneously advanced by and assigned to Norwest at the time of closing, their RESPA claim is precluded.

As already discussed, the Eighth Circuit unequivocally found that the Chandlers failed to produce "*even a scintilla of evidence*" that Norwest was involved in their loan transaction. (Pet. App. 9) (emphasis added). The Majority specifically found that "the loan was sold by Custom to Equicon, *not* Norwest." (Pet. App. 8) (emphasis added). For this reason, the Chandlers' "table funding" argument necessarily fails, at least with respect to Norwest.

As for Custom, the uncontroverted evidence shows that it closed the Chandler loan in its own name and funded it with its wholesale line of credit from CoreStates Bank. Custom was

solely liable for the funds until Equicon purchased the Chandler loan after closing. (Pet. App. 8). Under the applicable RESPA regulation, this exact type of arrangement is an exempt secondary market transaction rather than "table funding:"

> The following illustrations provide additional guidance on the meaning and coverage of the provisions of RESPA....
>
> . . .
>
> 5. *Facts:* A, a "mortgage originator," receives loan applications, funds the loans with its own money or with a wholesale line of credit for which A is liable, and closes the loans in A's own name. Subsequently, B, a mortgage lender, purchases the loans and compensates A for the value of the loans, as well as for any mortgage servicing rights.
>
> *Comments*: Compensation for the sale of a mortgage loan and servicing rights constitutes a secondary market transaction, rather than a referral fee, *and is beyond the scope of Section 8 of RESPA*. For purposes of Section 8, in determining whether a *bona fide* transfer of the loan obligation has taken place, HUD examines the real source of funding, and the real interest of the named settlement lender.

See 24 C.F.R. Part 3500, Appendix B (emphasis added). Accordingly, the Majority correctly found that "the Chandlers have failed to produce any evidence that the [funds] disbursed to them in connection with their mortgage loan came from any source *other than Custom.*" (Pet. App. 7) (emphasis added).

It was precisely this finding by the Majority that prompted Judge Gibson's dissent. Rather than apply the RESPA regulation as promulgated, however, he applied his own definition of a "secondary market transaction." Specifically, he reasoned that because Custom and Equicon followed a "preordained procedure" to ensure that the deal complied with 24 C.F.R. Part 3500,

it constituted a "sham transaction designed to avoid coverage under RESPA." (Pet. App. 12).

Norwest is not in a position to speculate the reasons why Custom and Equicon structured the transaction the way they did. It would seem, however, that one obvious purpose for the RESPA regulation is to provide guidance to the mortgage industry as to what types of transactions will—and will not—be subject to RESPA scrutiny, so that the industry may structure its transactions accordingly. The Eighth Circuit correctly applied the RESPA regulation as promulgated, and the Chandlers' Petition for Certiorari should be denied. *See* Supreme Court Rule 10 ("A petition for a writ of certiorari is *rarely granted* when the asserted error consists of...the misapplication of a properly stated rule of law.") (emphasis added).

3. THE EIGHTH CIRCUIT PROPERLY AFFIRMED RULE 11 SANCTIONS.

The Chandlers challenge the Eighth Circuit's affirmance of the Rule 11 sanctions, arguing that Judge Gibson's dissent shows that "there is no consensus that the Chandlers' legal theory is invalid and, therefore, sanctionable." (Pet., p.12). While this might be true with respect to the Chandlers' theory of "table funding," it is *not* true with respect to their baseless allegations against Norwest. Regardless whether Custom "table funded" the loan for Equicon, the Chandlers have absolutely *no* claim against Norwest, given its demonstrated lack of involvement in the loan transaction. (Pet. App. 9). Accordingly, the Eighth Circuit properly reviewed and affirmed the District Court's discretion to impose Rule 11 sanctions due to the Chandlers' attorneys' failure to investigate the facts prior to filing this lawsuit. *Cooter & Gell,* 496 U.S. at 405 ("an appellate court should apply an abuse-of-discretion standard in reviewing all

aspects of a district court's Rule 11 determination").[3]

Indeed, the Chandlers expressly admitted in their appellate briefs that they joined Norwest in this action based upon their attorneys' "*inferences*" about Norwest's potential role in the transaction, and *not* upon the pre-filing inquiry mandated by Rule 11. (Appellants' Response Brief at 21). "[P]laintiffs' counsel are experienced in mortgage industry litigation," explained the Chandlers. "Attorneys are often more familiar with industry practices than courts." (*Id.* at 20-21). But this is no justification for wrongfully joining Norwest in this lawsuit—particularly given Norwest's immediate (and repeated) advice to the Chandlers' attorneys that it lacked any involvement in their clients' loan transaction. Accordingly, the Eighth Circuit's affirmance of Rule 11 sanctions against the Chandlers' attorneys is beyond reproach.

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[3] "[A]n abuse of discretion only occurs where no reasonable person could take the view adopted by the trial court. If reasonable persons could differ, no abuse of discretion can be found." *Durr v. Intercounty Title Co. of Illinois*, 14 F.3d 1183, 1187 (7th Cir.), *cert. denied*, 513 U.S. 811 (1994).

CONCLUSION

In *Durr v. Intercounty Title Co. of Illinois*, 14 F.3d 1183 (7th Cir.), *cert. denied*, 513 U.S. 811 (1994), this Court denied a petition for certiorari where the Seventh Circuit had affirmed Rule 11 sanctions against a plaintiff's attorney who filed a RESPA class action "without conducting any factual inquiry—that Intercounty's overcharge to Durr was not an isolated incident; he *surmised* that if Intercounty overcharged Durr, it must have overcharged others." *Id.* at 1186 & 1187-88 (emphasis added).

Precisely as in *Durr*, the Chandlers' attorneys impermissibly "inferred" that Norwest was involved in their clients' loan transaction, and immediately filed this RESPA class action without conducting the necessary factual inquiry. They inexcusably compounded this error by refusing to abandon their claims against Norwest long after being advised of Norwest's lack of involvement. Accordingly, Norwest respectfully requests this Court to deny the Chandlers' baseless Petition for Certiorari, and, pursuant to Supreme Court Rule 42.2, order the Chandlers' attorneys to pay Norwest's fees and costs incurred to oppose the Petition.

Respectfully submitted,

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